

Message Text

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R 250823Z MAY 74

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TO SECSTATE WASH DC 2811

INFO AMEMBASSY HELSINKI

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TAGS: ECON, OECD

SUBJECT: EDRC ANNUAL REVIEW OF FINLAND, MAY 21

REFS: (A) USOECD 12007

(B) OECD DOCUMENT EDR(74)12

1. SUMMARY: EDRC ANNUAL REVIEW OF FINLAND ON MAY 21 WAS GENERALLY UNEXCEPTIONAL AFFAIR WITH FINNISH TEAM UNABLE RESPOND TO MANY QUESTIONS AND FREQUENTLY ASKING COMMITTEE FOR SUGGESTIONS ON FUNDAMENTAL POLICY ISSUES. FINNS WERE MORE OPTIMISTIC THAN SECRETARIAT REGARDING DEMAND OUTLOOK FOR REMAINDER 1974, AND HAVE REVISED UPWARDS THEIR FORECASTS FOR MAJOR DEMAND COMPONENTS. PRINCIPAL CONSTRAINT WILL BE ON SUPPLY SIDE, WHERE BOTTLENECK EXPECTED HOLD GNP GROWTH TO 3.5 PERCENT. CPI EXPECTED GROW 14 PERCENT. CURRENT ACCOUNT DEFICIT OF 3 TO 3.5 BILLION MK WILL BE LARGER THAN EXPECTED, BUT IMPACT WILL BE SOFTENED BY MEDIUM-TERM PAYMENTS ARRANGEMENTS WITH USSR. MAIN PROBLEM FOR FINLAND WILL BE RE-ALLOCATION OF RESOURCES TO EXPORT SECTOR WHERE CAPACITY CONSTRAINTS LIMIT FINNISH ABILITY TO RESPOND TO

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STRONG EXTERNAL DEMAND. END SUMMARY.

2. DEMAND OUTLOOK. ALTHOUGH FINNS CONTINUE TO EXPECT ECONOMY TO SLOW DOWN AS YEAR PROGRESSES, THEY ARE NOW MORE OPTIMISTIC THAN IN EARLIER FORECASTS. NEW ESTIMATES SEE CONSUMER DEMAND RISING AT 3 PERCENT, EXPORT DEMAND UP 5 PERCENT, AND GDP RISING BY 3.5 PERCENT. FINNS NOW THINK DEMAND WILL BE SUFFICIENT TO MAINTAIN EMPLOYMENT AT ACCEPTABLE LEVELS. MAIN PROBLEM WILL BE SUPPLY BOTTLENECKS WHICH NOT ONLY ARE CONTRIBUTING TO DEMAND PULL INFLATION BUT ALSO ARE PREVENTING FINLAND FROM RESPONDING TO STRONG EXPORT DEMAND. OIL IMPACT ON DOMESTIC DEMAND WILL NOT BE AS SEVERE AS IN OTHER OECD COUNTRIES, SINCE MOST OIL IMPORTS CAME FROM USSR UNDER BILATERAL TRADING AGREEMENTS. SECRETARIAT SAW NO NEED FOR EXPANSIONARY DOMESTIC POLICIES, BECAUSE USSR DEMAND FOR FINNISH EXPORTS WILL PROVIDE NECESSARY STIMULUS.

3. PRICES AND WAGES. CONSUMER PRICES EXPECTED INCREASE 14 PERCENT IN 1974, OF WHICH 6 PERCENTAGE POINTS DUE TO INCREASED IMPORT PRICES. FINNS ARE PLACING MAIN RELIANCE ON PRICE AND WAGE CONTROLS TO CONTROL INFLATION. RECENT CENTRALIZED INCOMES AGREEMENT WAS MOTIVATED BY THIS CONCERN, SINCE WITHOUT SUCH AGREEMENT FINNS EXPECTED MUCH GREATER WAGE DEMANDS FROM INDIVIDUAL UNIONS. REGARDING PROMISED REDUCTION IN INCOME TAXES WHICH GOVERNMENT OFFERED AS COMPENSATION FOR MORE RESTRAINED WAGE DEMANDS, FINNS DID NOT AGREE WITH SECRETARIAT THAT THIS WOULD INVOLVE LOSS OF FLEXIBILITY IN PURSUING FISCAL POLICY, SINCE TAX RATE CHANGES HAVE NOT TRADITIONALLY BEEN USED AS FISCAL WEAPON.

4. BALANCE OF PAYMENTS. FINNS EXPECT CURRENT ACCOUNT DEFICIT TO BE BETWEEN 3 AND 3.5 BILLION MK, PRIMARILY DUE TO WORSENING TERMS OF TRADE ON OIL ACCOUNT VIS-A-VIS

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USSR. APPROXIMATELY TWO THIRDS OF OIL IMPORTS COME FROM USSR AND SOMEWHERE BETWEEN ONE THIRD AND ONE HALF OF CURRENT DEFICIT WILL BE ON BILATERAL TRADE ACCOUNT. HOWEVER, SINCE PAYMENTS TO SOVIETS IN REAL GOODS CAN BE MADE ON FLEXIBLE SCHEDULE OVER FIVE-YEAR PERIOD, IT WOULD NOT BE NECESSARY TO DIVERT EXPORTS FROM CONVERTIBLE CURRENCY MARKETS. AT PRESENT, MAIN PROBLEM IN MEETING INCREASED EXPORT DEMAND FROM ALL SOURCES IS LACK OF SPARE CAPACITY IN EXPORT SECTOR.

5. U.S. DEL ASKED HOW FINNS EXPECT TO SHIFT RESOURCES TO EXPORT SECTOR IN ORDER TO RESOLVE SUPPLY BOTTLENECKS. FINNS UNABLE TO REPLY AND ASKED COMMITTEE FOR SUGGESTIONS REGARDING MEASURES TO RE-ALLOCATE RESOURCES. SECRETARIAT (ANDERSEN) SUGGESTED THAT PRIMARY CANDIDATE SHOULD BE PRIVATE CONSUMPTION WHICH COULD BE RESTRICTED PERHAPS BY RAISING INDIRECT TAXES OR INCREASING INTEREST RATES. HE NOTED THAT PRESENT PLAN TO REDUCE TAXES AS PART OF INCOMES PACKAGE WOULD HAVE OPPOSITE EFFECT. FINNS OBJECTED THAT BOTH MEASURES WOULD HAVE INFLATIONARY LIMITED OFFICIAL USE

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IMPACT. U.S. DEL SUGGESTED THAT FINNS MIGHT EMPLOY SELECTIVE CREDIT CONTROLS, WHICH FINNS ADMITTED WAS ONE POSSIBILITY UNDER CONSIDERATION.

6. FINNISH PLANS FOR FINANCING CURRENT ACCOUNT DEFICIT INCLUDE STANDBY FACILITY WITH FOREIGN CENTRAL BANKS AMOUNTING TO 1.2 BILLION MK. THIS WOULD LEAVE APPROXIMATELY 1 BILLION MK IN CONVERTIBLE CURRENCY DEFICIT TO BE FINANCED, AFTER EXCLUDING PORTION ATTRIBUTABLE TO BILATERAL TRADE WITH USSR. THEY INDICATED PREFERENCE FOR LONG-TERM FINANCING, BUT NOTED THAT MEASURES MIGHT HAVE TO BE TAKEN TO ENCOURAGE SHORT-TERM CAPITAL INFLOWS.

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